

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

IN RE DERIVATIVE LITIGATION,	:	CIVIL ACTION
HERLEY INDUSTRIES INC.	:	
	:	No. 06-02964
	:	

MEMORANDUM

Juan R. Sánchez, J.

April 11, 2007

Defendants ask for a stay of the civil proceedings to avoid any undue prejudice against Defendants Herley Industries, Inc. and Lee Blatt in the parallel criminal case. Plaintiffs argue any prejudice to Herley's and Blatt's criminal case can be avoided by staying the civil case against Blatt alone. Weighing the relevant factors, I find Defendants Herley and Blatt will not risk prejudice to their criminal case until after the Motions to Dismiss are decided and, therefore, reserve ruling on the three Motions to Stay until after I rule on the Motions to Dismiss.

FACTS

On June 6, 2006, a grand jury sitting in the Eastern District of Pennsylvania indicted Lee Blatt and Herley Industries, Inc., alleging twenty-nine counts of wire fraud, two counts of obstruction of a federal audit, one count of major fraud against the United States, and three counts of false statements to the government. The grand jury returned a superseding indictment on January 30, 2007, which amended the wire fraud charges. The indictment alleges Blatt and Herley defrauded the government in connection with Herley's bid for contracts to provide certain electronic components to the military by submitting fraudulent price quotations and fraudulent support for

those quotations. Both Blatt and Herley have entered pleas of not guilty on all counts. The criminal trial is scheduled for January 15, 2008.

Shortly following the indictment, on June 15, 2006, plaintiff Kevin Montoya filed a securities class action suit against Herley, Blatt, and Herley executives. On July 6, 2006, Plaintiff Michelle Blair filed this suit as a derivative action against Herley, Blatt, and members of Herley's board of directors.

DISCUSSION

When a litigant or witness in a civil matter faces criminal charges, a district court has the discretion to stay discovery, in whole or in part, until the disposition of the criminal matter. *RAD Services, Inc. v. Aetna Surety and Casualty Co.*, 808 F.2d 271, 279 n.3 (3d Cir. 1986). “[T]he power to stay proceedings is incidental to the power inherent in every court to control the disposition of the cases on its docket with the economy of time and effort for itself, for counsel, and for litigants. How this can best be done calls for the exercise of judgment, which must weigh competing interests and maintain an even balance.” *Landis v. North American Co.*, 299 U.S. 248, 254-55 (1936) (citing *Kansas City Southern R. Co. v. United States*, 282 U.S. 760, 763 (1931)); see *Texaco, Inc. v. Borda*, 383 F.2d 607, 608 (3d Cir.1967) (quoting same). The stay of a civil case is an extraordinary remedy. *Trustees v. Transworld Mechanical*, 886 F. Supp. 1134, 1139 (S.D.N.Y. 1995); *Weil v. Markowitz*, 839 F.2d 166, 174 n.17 (D.C.Cir. 1987). The decision to stay civil proceedings calls for the trial court, in its discretion, to balance the various interests of the parties, the court, and the public. *Landis*, 299 U.S. at 254-56.

As threshold matters, many courts look to determine the extent to which the issues in the criminal and civil cases overlap and the status of the criminal case, including whether the defendants

have been indicted. *Volmar Distributors, Inc. v. New York Post Co., Inc.*, 152 F.R.D. 36, 39 (S.D.N.Y. 1993) (citing Judge Milton Pollack, *Parallel Civil and Criminal Proceedings*, 129 F.R.D. 201, 203 (S.D.N.Y. 1989) (“The most important factor at the threshold is the degree to which the civil issues overlap with the criminal issues.”)). Although the case for a stay is the strongest where a civil defendant has been indicted and the issues are similar, “[i]t is still possible’ to obtain a stay even though an indictment or information has not yet been returned” *Walsh Securities, Inc. v. Cristo Property Management, Ltd.*, 7 Supp. 2d 523, 527 (D.N.J. 1998) (quoting *Parallel Proceedings*, 129 F.R.D. at 204). It is important to consider the status of the criminal case early in the analysis because parallel proceedings may have the effect of undermining a defendant’s Fifth Amendment privilege against self-incrimination, expanding the scope of criminal discovery beyond the limits of Rule 16(b) of the Federal Rules of Criminal Procedure, exposing the basis of the defense to the prosecution in advance of trial, or otherwise prejudicing the criminal case. *Volmar Distributors*, 152 F.R.D. at 39 (citing *S.E.C. v. Dresser Industries, Inc.*, 628 F.2d 1368, 1376 (D.C.Cir.), *cert. denied*, 449 U.S. 993 (1980)).

It is undisputed Defendants Herley and Blatt have both been indicted. Although there are numerous individual defendants, Blatt’s criminal activities are central to the civil case. The Complaint is based on the same events that give rise to the criminal charges contained in the Indictment. Both the Complaint and the Indictment focus on the conduct of Blatt and Herley in relation to the bid process for certain electronic components supplied to the military, the government pre-award audits of those bids, execution of the relevant contracts, and the Department of Defense investigation arising out of those transactions. Thus, I find there is substantial overlap between the civil and criminal proceedings.

Turning next to the balancing of the interests, relevant factors for the Court to consider are (1) the interest of the plaintiff in proceeding expeditiously with his case and any potential prejudice it may suffer from any delay; (2) the burden upon the defendants from going forward with any aspects of the proceedings, in particular any prejudice to their rights; (3) the convenience of the court and the efficient management of judicial resources; (4) the interests of any non-parties; and (5) the interest of the public in the pending civil and criminal litigation. *See, e.g., Golden Quality Ice Cream Co. v. Deerfield Specialty Papers, Inc.*, 87 F.R.D. 53, 56 (E.D.Pa.1980) (Louis Pollak, J.). The Court is to consider these factors “with the basic goal being to avoid prejudice.” *Volmar Distributors*, 152 F.R.D. at 39.¹

This balancing begins by considering the prejudice to the plaintiffs if the case is delayed. Evaluating this prejudice, courts may insist the plaintiff establish more than simply a delay in his right to expeditiously pursue his claim. *Golden Quality Ice Cream*, 87 F.R.D. at 56. Instead, the plaintiff should demonstrate a unique injury, such as the dissipation of assets or an attempt to gain an unfair advantage from the stay. *See, e.g., State Farm Mut. Automobile Ins. Co. v. Beckham-Easley*, 2002 WL 31111766, at *3 (E.D. Pa. Sept. 18 2002); *Walsh Securities*, 7 F. Supp.

¹ Other courts have considered the threshold factors as prongs to be weighed with the five factor test listed above. *See e.g. Adelphia Communications Securities Litigation*, 2003 WL 22358819, at *3 (E.D. Pa. May 13, 2003), *State Farm Mut. Automobile Ins. Co. v. Beckham-Easley*, 2002 WL 31111766, at *1 (E.D. Pa. Sept. 18 2002), *Walsh Securities*, 7 Supp. 2d 523, 526-27. While the status of the criminal case and the overlap between the civil and criminal cases are important considerations, these threshold factors are most appropriately considered early in the analysis, before moving to the five-factor balancing test. The purpose of the threshold factors should be to determine whether the defendant will have a credible claim his or her constitutional rights may be jeopardized by parallel proceedings. This is best done early to weed out those cases where the Defendant is unlikely to be prejudiced by the parallel proceedings. *Paine Webber, Jackson & Curtis, Inc. v. Malon S. Arduis, Inc.*, 486 F. Supp 1118, 1119 (S.D.N.Y 1980) (“Absent a showing of undue prejudice upon defendant or interference with his constitutional rights, there is no reason why plaintiff should be delayed in its efforts to diligently proceed to sustain its claim.”).

2d at 528. Here, the Plaintiffs have articulated no unique injury citing only continued monetary loss and the passage of time.

I next consider the Defendants' burden if the civil case is allowed to proceed. As noted above, civil defendants subject to a criminal indictment must often choose between waiving their Fifth Amendment rights during civil discovery or asserting the privilege and losing the civil case. *Walsh Securities*, 7 F. Supp. 2d at 528. While it is not unconstitutional to place a defendant in this position, *Baxter v. Palmigiano*, 425 U.S. 308, 318-19 (1976), courts may consider these conflicts when deciding whether to stay a civil case. *Dresser Indus.*, 628 F.2d at 1375. Refusing to grant a stay might also expand the rights of criminal discovery beyond the limits of Federal Rule of Criminal Procedure 16(b), expose the basis of the defense to the prosecution in advance of trial, or otherwise prejudice the criminal case. *Volmar Distributors*, 152 F.R.D. at 39 (citing *id.* at 1376).

Here, Defendants argue Blatt will be forced to choose whether to assert his fifth amendment right or lose his civil case if the case is allowed to continue. They also argue denying the Motions to Stay would give the prosecution a preview of their defense strategies and prejudice the criminal case against them. Although Herley admits a corporate entity does not have a Fifth Amendment right against self-incrimination, *Braswell v. United States*, 487 U.S. 99, 100 (1988), it too argues it would be unfairly prejudiced if the prosecution were privy to its defense strategy. The remaining individual defendants argue denial of the stay would prejudice their interests because Blatt would be virtually inaccessible. While I am persuaded answering the Complaint and certain discovery would be seriously burdensome to Blatt, this burden is trivial at the Motion to Dismiss stage because the Motions to Dismiss do not implicate the criminal charges. As the parties admitted during oral argument, the prejudice to Blatt's Fifth Amendment rights, and the risk of exposing the Defendants'

legal strategies to the prosecution, are absent until Blatt is forced to answer the Complaint.² “[A]bsent a showing of undue prejudice upon defendant or interference with his constitutional rights, there is no reason why plaintiffs should be delayed in their efforts to diligently proceed to sustain their claim.” *Arden Way Associates v. Boesky*, 660 F.Supp. 1494, 1497 (S.D.N.Y. 1987) (Milton Pollack, J.).

Turning next to the interest in judicial efficiency, I am concerned a stay at this point would unnecessarily delay prompt resolution of the civil claims. As I explained, there is no danger Blatt’s Fifth Amendment rights will be jeopardized or the Defendants’ legal strategies will be revealed to the prosecution, before the Motions to Dismiss are decided. The parties are currently on track to argue the Motions to Dismiss in June, 2007. Given the nature of the Motions, and the parties’ representations the Motions will not implicate Blatt’s Fifth Amendment right, I find it is in the interest of judicial efficiency to proceed with the case until after I rule on the Motions to Dismiss.

Considering the fourth prong, neither party has suggested any third-party rights would be prejudiced by a stay in this case. I will not weight this factor in my analysis.

Finally, I briefly note the important public interest in prompt resolution of securities claims. “Indeed, the public interest in the integrity of securities markets militates in favor of the efficient and expeditious prosecution of these civil litigations.” *Arden Way*, 660 F. Supp. at 1500. “To this end it would behoove both the litigants and the court to tailor a stay at the instance of the defendant . . . to minimize any delays upon the process.” *Parallel Proceedings*, 129 F.R.D. at 205. Given the lack of undue prejudice to the defendants or inference with Blatt’s constitutional rights until after

² The Plaintiffs have agreed to stay the case against Blatt until the criminal case is resolved. While I do not believe a stay of the proceedings against Blatt is necessary at this time, I will revisit this suggestion after I rule on the Motions to Dismiss.

I rule on the Motions to Dismiss, I am persuaded the case should not be stayed at this time.

An appropriate order follows.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

IN RE DERIVATIVE LITIGATION,	:	CIVIL ACTION
HERLEY INDUSTRIES INC.	:	
	:	No. 06-02964
_____	:	

ORDER

And now this 11th day of April, 2007, it is hereby ORDERED judgment on Defendants' Motions to Stay Civil Proceedings (Documents 17, 19, 20) is hereby RESERVED. Plaintiff Michelle Blair's MOTION for Relief (Document 31) is hereby DENIED. In the event the trial in Herley Industries, Inc.'s and Lee Blatt's criminal case is postponed, within five days of the postponement, counsel for Mr. Blatt shall advise the court and opposing counsel of the status of the trial date.

BY THE COURT:

/s/ Juan R. Sánchez
Juan R. Sanchez, J.